IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 32 of 1987

For Approval and Signature:

Hon'ble MR.JUSTICE A.R.DAVE Sd/-
and
Hon'ble MR.JUSTICE D.A.MEHTA Sd/-

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : YES

2. To be referred to the Reporter or not? : YES

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

KAIRA DIST. CO.OP.MILK PRODUCERS UNION LTD.
Versus
COMMISSIONER OF INCOME-TAX

Appearance:
MR JP SHAH for Applicant.
MR AKIL QURESHI FOR MR MANISH R BHATT for Respondent

CORAM : MR.JUSTICE A.R.DAVE
and
MR.JUSTICE D.A.MEHTA

Date of decision: 02/07/2001

ORAL JUDGEMENT

(Per : MR.JUSTICE D.A.MEHTA)

1 The Income-Tax Appellate Tribunal, Ahmedabad Bench 'C' has referred the following three questions for the opinion of this Court u/s.256(2) of the Income-Tax Act,1961 (hereinafter referred to as 'the Act').

"(i) In the facts and circumstances of the case whether the Appellate Tribunal was right in its interpretation and application of Section 35C of the Income-tax Act,1961 ?

(ii) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that the entire expenditure of Rs.43,69,466/- for A.Y.1978-79 was not eligible for weighted deduction under section 35C?

(iii) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that only 10% of the expenses incurred on dissemination of information or demonstration of modern techniques and the methods of agricultural, animal husbandry or dairy or poultry farming or advice on such techniques or methods, is eligible for weighted deduction u/s.35C of the Act ?"

2. The assessee-applicant is the Union of Cooperative Societies engaged in marketing of milk and milk products. For assessment years 1977-78 and 1978-79, the relevant previous years are years ended on 31/3/1977 and 31/3/1978 respectively. For the aforesaid two assessment years, the assessee claimed deduction u/s. 35C of the Act in relation to the following expenses :

	A.Y. 77-78.	A.Y.78-79.
Salary of Veterinary Doctors.	11,62,120	12,25,772
Veterinary medicines	11,70,717	14,80,924
Veterinary transport	16,29,596	13,66,040
Artificial Insemination Exp.	2,61,808	3,81,720

Development & Research exps.	2,56,700	1,08,400
Fodder growing expenses	2,30,938	3,66,449
Amul patrika expenses	67,587	71,509

3. The Income Tax Officer during the course of assessment proceedings allowed the deduction in relation to the last item being 'Amul Patrika' Expenses. Against the disallowance of the rest of the items the assessee went in appeal before the Commissioner of Income Tax (Appeals) who for the reasons stated in his order confirmed the assessment order. The assessee being aggrieved by the aforesaid Appellate Authority's order preferred appeals for both the years before the Income-Tax Appellate Tribunal and the Tribunal vide its order dated 18/1/1984 restored the disallowance in relation to development and research expenses for the reasons stated in para 8 of its order to the file of the Income-Tax Officer for adjudication. Therefore, we are not called upon to opine in relation to the aforesaid item also. In other words whether salary of veterinary doctors, expenditure for veterinary medicines, veterinary transport, artificial insemination expenditure, and fodder growing expenses would fall within the nature of expenses envisaged by the provisions of section 35C of the Act and would be eligible for deduction has to be considered. It is pertinent to note that the Tribunal has held, in relation to all these items, that 10% of the total expenses claimed would be eligible for weighted deduction u/s.35C of the Act.

4. According to the Tribunal on an analytical summary of the activities carried out by the assessee, it was found that the assessee was engaged in providing technical services. It further held that the assessee was engaged in supplying material and conducting various operations through its own staff in the designated villages. Thus, according to the Tribunal, the activities carried on by the assessee could not be said to be governed by the provisions of section 35C(1)(b)(ii) of the Act. The Tribunal further observed that " it may be true that the cattle owners would learn from the operations carried out but that is only incidental."

5. Assailing the aforesaid findings of the Tribunal Mr.J.P.Shah, learned Advocate for the assessee submitted that the provision does not envisage any concept of "incidental benefit" and the Tribunal was in error in

importing the said concept in its reasoning. It was further submitted that for the purpose of deciding the issue a liberal construction of the provision should be adopted bearing in mind the object for which the provision was enacted. In support of this reliance was placed on the Supreme Court decision in the case of C.I.T. Vs. Cynamid India Ltd., 237 I.T.R.585. Mr.Shah also relied upon the decisions in the case of Indian Leaf Tobacco Development Co.Ltd. Vs. C.I.T., 137 I.T.R.827 (Kolkatta) and in the case of C.I.T. vs. Navabharat Enterprises Pvt.Ltd.,165 I.T.R.603 (A.P.) in support of his submissions.

6. Mr.Akil Qureshi, learned Counsel appearing on behalf of the revenue, while supporting the order of the Tribunal submitted that the purpose of the provision will have to be taken into consideration while answering the query as to whether the assessee society is imparting information to the cultivators or is it carrying on the activity itself. Elaborating on the said submission it was contended that in the case of the assessee dissemination of information or demonstration of modern technique was absent and in fact the work was carried out by the assessee itself through its own agency. It was further submitted that the activities were of such a nature that it was not possible for an individual farmer or a cultivator to undertake such activities on his own. Mr.Qureshi further submitted that on analysis of provision of section 35C(1)(b) it was clear that sub-clause (i) pertained to only goods and sub-clause (ii) was applicable only in case of services and facilities. It was further contended that the expenditure in question would qualify for deduction only if there was dissemination of information or demonstration or advice of modern techniques and methods as specified in the said sub-clause and not in relation to any other activity.

7. The revenue's case is that dissemination of information or demonstration of, modern techniques or methods of agriculture, animal husbandry, dairy or poultry farming should be of such a nature so as to benefit the cultivator, grower or producer in such a way that it would enable the recipient to adopt such method or technique on its own and not when it becomes necessary for the supplier to continue to supply such services or facilities. It was submitted that in the present case the services provided by the assessee were of such magnitude and nature that it was not possible to state that the same amounted to either dissemination of information on modern techniques, or that they were

demonstration of modern methods or that any advice as such was rendered to the cultivators; to the contrary, it was an activity by which the assessee provided certain services which could not be availed of by the cultivator when an establishment like one the assessee was maintaining was not available. It was, therefore, contended that the Tribunal had rightly stated that the benefit, if any, derived by the cultivator, grower or producer was incidental, in as much as he may learn something by observing the method adopted by the agency of the assessee but would not be in a position to undertake such activity on his own, and therefore, the assessee was not entitled to deduction claimed as it did not fulfill the qualifying criteria.

8. The provisions of section 35C of the Act were introduced by the Finance Act,1968 with effect from 1/4/1968 and were made applicable only in case of Companies. The provisions were extended to Cooperative Societies by Taxation Laws (Amendment) Act,1975 for and from assessment year 1976-77. The provisions as they existed from 1/4/1968 upto 31/3/1984 provided for a weighted deduction being one and one-fifth times in case the expenditure was incurred for the purpose which was provided in the section. The relevant provisions are reproduced hereunder :

"Agricultural development allowance.

35C. (1)(a) Where any company [or a co-operative society] is engaged in the manufacture or processing of any article or thing which is made from, or uses in such manufacture or processing as raw material, any product of agriculture, animal husbandry, or dairy or poultry farming, and has incurred, after the 29th day of February,1968, whether directly or through an association or body which has been approved for the purposes of this section by the prescribed authority, any expenditure in the provision of any goods, services or facilities specified in clause (b) to a person [not being a person referred to in clause (b) of sub-section (2) of section 40A] who is a cultivator, grower or producer of such product in India. [the company or co-operative society] shall, subject to the provisions of this section, be allowed a deduction of sum equal to one and one-fifth times the amount of such expenditure incurred during the previous year.

(b) The goods, services or facilities referred to in clause (a) are the following :-

(i) fertilizers, seeds, pesticides, concentrates for cattle and poultry feed, tools or implements, for use by such cultivator, grower or producer;

(ii) dissemination of information on, or demonstration of, modern techniques or methods of agriculture, animal husbandry, or dairy or poultry farming, or advice on such techniques or methods;

(iii) such other goods, services or facilities as may be prescribed.

Explanation : In computing the expenditure with reference to which deduction under this section is to be allowed, the amount, if any, received by [the company or co-operative society] in consideration of, or as compensation for, such goods, services or facilities shall be deducted.

(2) Where a deduction under this section is claimed and allowed for any assessment year in respect of any expenditure of the nature specified in sub-section (1), deduction shall not be allowed in respect of such expenditure under any other provision of this Act for the same or any other assessment year."

On analysis of the aforesaid section it can be seen that the allowance is provided in clause (a) of sub-section (1) of section 35C of the Act, while clause (b) only specifies the goods, services or facilities which have been referred to in clause (a) for ascertaining qualifying expenditure. The requisite conditions are :

(1) the assessee should use in manufacture or processing of any article or thing as raw material any product of agriculture, animal husbandry or dairy or poultry farming

(2) the assessee should have incurred expenditure for providing goods, services

or facilities after 29th day of February,1968 and such goods, services or facilities should be those as specified in clause (b),

(3) such goods, services or facilities have to be provided to cultivators, growers or producers of such product in India,

(4) the words 'such product' have direct reference to raw material viz., any product of agriculture, animal husbandry etc. and such raw material has to be used by the assessee in its manufacturing or processing activities.

The section further provides by way of Explanation that in case where a deduction under the section is to be allowed the qualifying expenditure shall be computed after reducing the same by consideration or compensation received by the assessee for supply of such goods, services or facilities. Sub-section (2) of Section 35C of the Act stipulates that where the deduction under this section is claimed and allowed no deduction shall be allowed in respect of such expenditure under any other provision of the Act for the same or in other assessment year.

9. When the provision was introduced in 1968, Central Board of Direct Taxes issued circular No. (LXXVI-66) of 1968 dated 6/7/1968. Para 56 of the said circular is reproduced hereunder as it draws distinction between agro-based industries and agro industries :

"The weighted deduction has been provided only in the case of companies engaged in agro-based industries, i.e. those which use as raw material, or process, the products of agriculture, animal husbandry, dairy or poultry farming. Accordingly, companies which are engaged in agro-industries (as distinct from those engaged in agro-based industries) such as those manufacturing, fertilizers, seeds, pesticides, tractors, implements, etc., are not eligible for the weighted deduction even though they may incur expenditure on supply of fertilizers, seeds, pesticides, tractors or other implements to the farmers or on demonstration of the use of these products for their benefit. This is because such expenditure would be

incurred by these companies as part of their sales promotion effort and it is not the intention to allow a weighted deduction in relation to expenditure on such activities. The weighted deduction will also not be available where the company engaged in an agro-based industry owns its own farm and incurs expenditure on seeds, fertilizers, etc., used for the cultivation of such farm."

10. That brings us to the aspect of determination of qualifying expenditure. Section 35(1)(b) specifies vide sub-clause (i) the goods which qualify to be considered for the purpose of determination whether a deduction is available under clause (a) of sub-section (1); sub-clause (ii) specifies services and facilities and sub-clause (iii) states as regards such other goods services or facilities as may be prescribed. Rule 6A(2) of the Income Tax Rules,1962, has prescribed the following goods and services :

"(i) dissemination of information on , or demonstration of, modern techniques or methods of processing, marketing and storage of seeds;

(ii) services or facilities given to seed growers for the purposes of storage, transport and insurance of seeds."

11. The assessee in the present case is a cooperative society engaged in manufacture or processing of milk and milk products which are made from milk as raw material. Such milk as raw material is derived by it from the person possessing cattle, through the society of which such a cattle owner is a member; the said society in turn is a member of the assessee which is a union of such cooperative societies. The assessee has incurred certain expenditure in the provision of certain goods, services or facilities and it is the assessee's case that the same have been provided to persons who are supplying raw material to the assessee. In so far as these facts are concerned both parties are at ad idem, the only dispute being as to whether the services or facilities provided by the assessee could be said to fall within sub-clause (ii) of clause (b) of sub-section (1) of section 35C of the Act. The provision of goods, services or facilities referred to in sub-clauses (i) and (ii) of clause (b) though apparently seem to fall in entirely different fields, yet are of such nature that there is every

likelihood of overlapping and it cannot be stated that there is any area which could not be governed by one or the other. Mr.Qureshi, learned Counsel for the revenue accepted this position but hastened to add that in the present case assessee's claim was under sub-clause (ii) of clause (b) and the activities were of such nature that they did not fulfill the requirements laid down by the statute.

12. Clause (a) of sub-section (1) of section 35C provides for deduction and it is in this clause that the nexus between the supplier of raw material to the assessee and the providing of service by the assessee has been stipulated. Though the nexus may not be direct yet the requirement is to the effect that the assessee to qualify for deduction shall incur expenditure of the specified nature to provide the goods, services or facilities to a person who would be in turn be the supplier of raw material. Underlying idea in the provision as can be culled out is that the assessee should incur expenditure for the purpose of obtaining raw material while at the same time incur such expenditure in a manner so as to undertake development of the recepient and the area in which the recepient is located i.e. rural area. If this test or the condition stands fulfilled then assessee would become entitled to claim weighted deduction as provided, with the aforesaid object in mind. The words used are " any expenditure" and thus are not limited to the nature of expenditure but the only limitation prescribed is in relation to specified goods, services or facilities. Therefore, merely because the assessee undertakes certain activities which may not directly disseminate information or demonstrate modern techniques or methods of either agriculture, animal husbandry, dairy or poultry farming it cannot be stated that the expenditure which is otherwise eligible for deduction does not fall within the nature of expenditure described in clause (a) of clause 35C of the Act. The restriction that the revenue wants to read in the provision does not flow from the language. The only requirement is that the person and the surrounding areas should benefit by way of development and the allowance i.e. weighted deduction is granted so as to subserve the purpose of development of the rural area. The contention that such development can take place only if the recepients are in a position to undertake such activities on their own and not otherwise is not borne out from the plain reading of the provision. The Explanation which lays down the mode of computing the eligible amount of expenditure is an inherent indicator to show that it is not necessary that the recipient of services or

facilities must himself imbibe the mode or the technique to the extent that the said recipient can himself undertake such activity. If that was the legislative intent it would not have been necessary to provide that the services or facilities should be compensated for and the eligible expenditure should be reduced to the extent of the consideration or compensation received.

13. In the case of the present assessee, it undertakes activities of artificial insemination, cross breeding etc., which would result ultimately in improving the breed of the milch cattle and as a consequence improve yield both in quantity and quality resulting in better supply of raw material to the assessee. In this situation, it cannot be stated that the purpose for which the section is enacted does not stand fulfilled, because, as stated, once the breed of milch cattle is improved there is development all around in relation to the recipient and the area in which such recipient is situated. At the cost of repetition we may state that it is not possible to read in sub-clause(ii) of clause (b) of sub-section (1) of section 35C of the Act, that the activities specified therein have to be restricted only for the limited purpose of educating the agriculturist, grower or producer and if over and above the process of educating such recipient some more services or facilities are rendered the assessee should be denied the benefit of weighted deduction u/s.35C of the Act.

14. In so far as the item of fodder growing expenditure is concerned the said activity would fall within sub-clause (i) of clause (b) in view of the fact that the assessee is actually distributing seeds fertilizers etc., and further providing proper irrigation facilities. The assessee is also undertaking levelling and developing the land which would also be an activity which would fall within the provision of services. Therefore, in relation to this item the assessee's claim would fall both within the provisions of sub-clauses (i) and (ii).

15. The Tribunal has held that the recipient of the service or facilities obtains incidental benefits or that the activities carried out by the assessee are of such a nature that the farmers would learn from the operation carried out only incidentally and thus 10% of the qualifying expenditure has been treated to be eligible for weighted deduction. The approach of the Tribunal is

unwarranted in as much as the provision does not permit bifurcating the allowable expenditure and thus there is no basis for holding that only 10% of such expenditure is allowable. Infact, there is no basis for holding so.

16. We, therefore, hold that the Appellate Tribunal was not right in its interpretation and application of section 35C of the Act. The first question referred to us is therefore answered in the negative i.e. in favour of the assessee and against the revenue. In so far as the second question is concerned the figure mentioned therein shall stand reduced in view of the fact that the expenses in relation to Amul Patrika have already been allowed by the Income Tax Officer and the expenditure relatable to development and research stands restored by the Tribunal to the file of the Income Tax Officer. The assessee is entitled to deduction of expenditure claimed in entirety except the aforesaid two items which have been dealt with by the Income Tax Officer. The second and third questions are accordingly answered in the negative i.e. in favour of the assessee and against the revenue.

17. Thus, the Reference stands disposed of accordingly with no order as to costs.

Sd/- Sd/-

(A.R.Dave, J) (D.A.Mehta, J)

m.m.bhatt